



Timothy Miller, CFA
Portfolio Manager
Ivy Small Cap
Value Fund

Finding value amid the chaos

In the five months Timothy Miller has managed Ivy Small Cap Value Fund, he has revamped the portfolio at a time when the small value investment category has been decidedly out of favor. Below, he talks about coming to Ivy Funds and the outlook for small value stocks. Mr. Miller has 29 years of industry experience, including four as CIO at Invesco Funds Group. He has managed small value portfolios for more than two decades.

Q: What is it about our investment culture that attracted you to our organization?

Miller: Ivy Fund's research reputation is excellent. Its traditional fundamental approach allows analysts to really get to know many industries, and its low portfolio manager turnover says there is an investment management culture where people really feel valued. I also have a lot of respect for Mike Avery. I worked with him in St. Louis, MO., at the start of my career (at Mercantile Bank's Mississippi Valley Advisors unit).

Q: What do you think of the daily morning investment meeting?

Miller: It gives me a complete investment overview that informs my decision-making. Many of the companies that get discussed are large cap and outside my typical investment parameters. However, the candid discussion of what's happening in that space, as well as across U.S. and global markets, is very instructive as I form my investment strategy. We're very good at identifying themes in the market and what might be worth emphasizing. I can take what I learn and apply it. Overall, I also think it's a good time to be in the small value space because it appears that many well-known investment firms are cutting back on their research staffs to cut costs and raise capital to compensate for huge write-offs. A growing number of small companies appear under-followed or are not followed at all.

Q: Can you provide some examples of market trends?

Miller: Recently we've seen economic sluggishness in Europe that's spread to Asia, and as a firm have taken a more cautious view about global growth. This has helped me analyze where I might have related exposure in the Ivy Small Cap Value Fund portfolio, and manage these risks, refine the portfolio, and avoid potential disappointments. At a sector level, Ivy has a great deal of expertise in soft commodities, and discussions regarding what is happening in industries such as agricultural chemicals have been very useful.

Past performance cannot guarantee comparable future results. Opinions expressed are those of Timothy Miller and are current as of September 2008. His views are subject to change at any time, based on market and other conditions, and no forecast can be guaranteed.

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Investors should consider the investment objectives, risks, charges and expenses of a fund carefully before investing. For a prospectus containing this and other information for the Ivy Funds, call your financial advisor or visit us online at www.ivyfund.com. Please read the prospectus carefully before investing.

Ivy Small Cap Value Fund

Discover Value That Others Miss

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Q: Small-cap value underperformed both large value and growth and small-cap growth for the 1-year period ended June 30, 2008, with the Russell 2000 Value Index falling 21.65 percent. When will the market turn in this space?

Miller: Having witnessed several economic cycles since 1979, I've seen that small value stocks are typically the first and hardest to fall going into an economic downturn, but they have also been among the first to rise at the start of a recovery. I think that just as the U.S. economy was the first to weaken globally in this cycle, it may be the first to come back. I believe that if you wait until GDP (gross domestic product) starts to tick up, you will have missed most of any rally in small value. Expectations are extremely low now, especially in the financial and consumer sectors, and I am finding it is a good time to be sorting through the rubble and focusing on high-quality companies. Snapback rallies for these stocks can be powerful, and we may see some companies move 30 to 50 percent fairly quickly once the market identifies a catalyst for recovery.

The criteria Ivy Small Cap Value Fund managers use to select and sell stocks

Valuation

- Price/earnings ratio (stock price divided by earnings per share)
- Price/book ratio (accounting value)
- Price/cash flow (stock price divided by operating profits)

Business Fundamentals

- High rate of return on equity
- Strong or weakening balance sheets
- Strong competitive position in an industry, or deterioration

Catalyst for Change

- Positive or negative earnings estimate revisions
- Improving working capital trends
- Catalyst for earnings improvement or deterioration

Q: What do you like currently?

Miller: Community banks in energy and agricultural regions, such as Texas, where the real estate market has held up better than it has nationally, appear attractive. I like counter-cyclical stocks in areas such as education, an industry that got hit by legislative and auction-rate problems a year ago, but now appears poised to do well as enrollment increases because of the downturn in employment. Trucking companies may benefit in the coming months because consolidation in this industry is occurring at a rapid pace, and they are beginning to see some relief in energy prices. Overall, I typically look for a catalyst that can unlock a company's value within a 12- to 18-month time frame.



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